Welcome to the Cuffelinks Newsletter

At any point in the investment cycle, there are experts waving red flags warning of market falls. In the depths of the GFC, few brave souls were buying the bargains while most investors were still looking for the exit amid fears of further losses.

What is your toehold?

In the current long global equity rally and with stretched company valuations, how defensive should a portfolio be? At the Portfolio Construction Forum Strategies Conference 2017 last week, Dr Robert Gay (pictured) led a discussion on '**Another global financial crisis is inevitable'**. Gay was Senior Economist for eight years at the Federal Reserve before founding Fenwick Advisers, and he said there are only three appropriate strategies for investors at the moment:

1. **Do nothing**, but expect to be a forced seller when prices fall
2. Focus on the **highest quality assets**, but they are already overpriced
3. Choose a **defensive strategy**, including sizing your exposures correctly and adding a 'short' component.

He also said falling prices will cause the next recession not the other way around; there's too much money chasing few quality, marketable assets; company pricing power has evaporated leaving flat inflation; a crisis exposes waste but we tend not to recognise it in advance; and investors need to focus on the correlations in their portfolios.

Most people will do nothing. Without suggesting this is red flag time, this week's edition focusses on the need for a toehold, starting with a 'base line' from Shane Oliver on what has happened since the GFC. Then Roger Montgomery invites comments on whether his market view is too bearish, and David Bassanese unpacks the current PE levels to see if the overpricing claim is justified.

On portfolios, Peter Wilmshurst sees value investing taking over from growth, while another value investor, Robert Miller, explains how to avoid 'value traps' in companies that look cheap.

Have you ever wondered why more fund managers do not use options to protect the downside in their portfolios? Simon Ho gives an 'as simple as possible' explanation into how options work.

All the ingredients but no recipe

Listening to economists often feels like receiving the ingredients to make a cake but no recipe, leaving investors more confused than ever. Guest acting economist Warren Peace III offers a cynical outlook in one sentence. Just don't expect any clarity.

Showing how precarious stock picking can be, the market reacted wildly to specific results last week. Bluescope fell 20%, Healthscope 17% and Vocus 23%, while BHP dug up 5%, a2 Milk rose a frothy 14%, Medibank a healthy 7% and Super Retail delivered 7%. Expect results from active fund managers to vary widely in the September quarter. The most-held stock in SMSF portfolios, Telstra, floated in 1997 at $3.30 a share and is now back to $3.60 after cutting its dividend.

Scott Morrison's plan

The Treasurer gave his annual Bloomberg address this morning and superannuation did not rate a mention. We can assume further changes are off the agenda at least for the life of this Government. While outlining his economic achievements, he said, "The reason for the rise in neo-liberalism and protectionism is the frustration still being felt on wages growth." His messages for 2018 will focus on "the politics of opportunity not the politics of envy", "new red Labor" and "tax to GDP ratios". A few years ago, it was difficult to find significant differences between Liberal and Labor policies, but that will not be the case going into the next election.

Finally, in this week's White Paper, Vanguard studies retirement transitions from the accumulation stage to post-retirement in four countries including Australia.

Graham Hand, Managing Editor